

Australian Equity Research

29 August 2016

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BUY

unchanged

PRICE TARGET A\$1.00

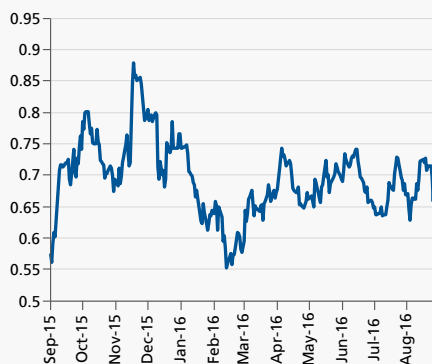
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Price (29-Aug) A\$0.73

Ticker SPL-ASX

| | |
|--------------------------------|--|
| 52-Week Range (A\$): | 0.54 - 0.98 |
| Avg Daily Vol (000s) : | 396.7 |
| Market Cap (A\$M): | 255 |
| Shares Out. (M) : | 367.1 |
| Enterprise Value (A\$M): | 209 |
| Last Cash Balance (A\$M): | 46.0 |
| Last Quarter Cash Burn (A\$M): | (5.7) |
| Major Shareholders: | Allan Gray Australia M&G Investments Fidelity Investment |

| FYE Jun | 2015A | 2016A | 2017E | 2018E |
|----------------------|--------|---------|--------|-------|
| Sales (A\$M) | 0.8 | 3.8↑ | 8.0 | 21.9 |
| Previous | 0.8 | 3.1 | 8.0 | 21.9 |
| PBT (A\$M) | (19.0) | (22.7)↓ | (13.3) | 2.9 |
| Previous | (19.0) | (17.4) | (13.3) | 2.9 |
| Net Income (A\$M) | (19.0) | (22.7)↓ | (13.3) | 2.9 |
| Previous | (19.0) | (17.4) | (13.3) | 2.9 |
| EPS (AUc) | (5.16) | (6.18)↓ | (3.63) | 0.78 |
| Previous | (5.16) | (4.75) | (3.63) | 0.78 |
| Cash Position (A\$M) | 30.8 | 46.0 | 32.6 | 35.5 |
| Previous | 30.8 | 46.4 | 33.1 | 35.9 |



SPL

Source: FactSet

SPL is developing new pharmaceutical, agrochemical and industrial products based on its proprietary dendrimer polymer technology.

Estimates Revised

Stars Aligning

Canaccord Genuity (Australia) Limited was a Joint Lead Manager to the Placement of 43.8M shares at A\$0.73 per share to raise ~A\$32M in December 2015.

Investment Perspective

SPL closed FY16 with cash of \$46.0M. The company posted net cash burn of \$17.8M with an operating cash burn of \$26.0M that was offset by \$4.1M received from customers, and a R&D tax rebate of \$3.4M. Receipts included a \$2.9M upfront payment from AstraZeneca (AZ) for a license to use SPL's DEP technology to improve a specific class of drugs. AZ has entered into second license to use DEP to improve an additional compound from its portfolio. We believe that both these licenses could generate additional cash payments from AZ during FY17. We also expect first commercial revenues from SPL's bacterial vaginosis (BV) application of VivaGel during FY17. On the back of strong news flow, the market could significantly re-rate SPL over the next 12 months. Hence, we maintain our **BUY** recommendation for SPL with a **A\$1.00 price target** that is based on a 12-year DCF (13.4% discount rate, no terminal value).

Key Points

Dendrimer nanoparticles starting to get bigger - FY16 has laid down the foundations for a big year in our view with its DEP nanoparticle drug delivery platform:

- during FY17, the company is likely to receive milestone payments from the first AZ license, which currently covers two drug candidates, as well as an upfront payment once the commercial terms of the second license are finalised;
- SPL should report data from the Phase-1 trial of DEP docetaxel by the end of 2016. Given the improved safety profile of the drug over native docetaxel, the company expects to initiate the first Phase-2 trial of DEP-docetaxel before the end of FY17;
- a second internal drug candidate should start clinical testing by the end of FY17. SPL has reported promising data from preclinical studies showing DEP-cabazitaxel had greater anti-cancer activity than the native drug without causing neutropenia;
- SPL also reported that dendrimers could act as highly effective scaffolds for antibody-drug conjugates (ADCs). In its annual report, the company has said it has signed two partnerships for this application of its dendrimers.

Going commercial with VivaGel for BV - we are expecting to see material progress from the VivaGel program for BV including first commercial returns during FY17:

- the company should announce data from the Phase-3 clinical trials for the prevention of BV in 1H 2017. If the results are positive, they should support a filing with the FDA;
- in July, the FDA issued new draft guidelines for BV drugs recommending that test of cure is evaluated at 7-14 days after treatment. As SPL's Phase-3 trials achieved this endpoint, the company may be able to file for FDA approval using existing clinical data.
- SPL signed a sales and marketing agreement with Aspen which should launch VivaGel in ANZ by year-end. Commercial partnerships for Europe and other markets should be signed by year-end with first sales expected in 2H FY17.

FINANCIAL SUMMARY

Financial Performance

| Year End | June | 2014A | 2015A | 2016A | 2017F | 2018F | 2019F | 2020F | 2021F | 2022F |
|-------------------------------|------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| VivaGel Condoms royalty | \$M | - | 0.3 | 0.1 | 0.3 | 0.9 | 2.0 | 3.6 | 5.1 | 8.4 |
| VivaGel - BV royalties | \$M | - | - | - | 0.7 | 5.1 | 10.4 | 21.2 | 43.0 | 72.9 |
| Drug delivery royalty | \$M | - | - | - | - | - | - | - | 5.6 | 11.3 |
| Agrochemicals royalty | \$M | - | - | - | - | 0.9 | 2.2 | 4.4 | 6.6 | 7.9 |
| Milestone payments | \$M | - | - | 2.9 | 7.0 | 15.0 | 30.0 | 35.0 | 75.0 | 50.0 |
| Other | \$M | 0.3 | 0.6 | 0.9 | - | - | - | - | - | - |
| Total product revenues | \$M | 0.3 | 0.8 | 3.8 | 8.0 | 21.9 | 44.6 | 64.2 | 135.3 | 150.4 |
| Interest revenue | \$M | 1.0 | 0.9 | 0.7 | 0.8 | 1.5 | 1.8 | 1.8 | 1.8 | 1.8 |
| Grants and tax rebates | \$M | 4.7 | 0.0 | 0.1 | 4.0 | 6.3 | 6.5 | 5.4 | 4.3 | 0.5 |
| Total revenue | \$M | 6.0 | 1.7 | 4.6 | 12.8 | 29.7 | 52.9 | 71.3 | 141.3 | 152.6 |
| R&D expenses | \$M | -11.0 | -16.3 | -22.2 | -20.0 | -20.5 | -18.0 | -9.5 | -1.0 | -0.5 |
| Administration expenses | \$M | -4.9 | -4.4 | -5.1 | -6.1 | -6.3 | -6.5 | -6.8 | -7.0 | -7.3 |
| Other expenses | \$M | - | -0.0 | -0.0 | - | - | - | - | - | - |
| Total expenses | \$M | -15.9 | -20.6 | -27.3 | -26.1 | -26.8 | -24.5 | -16.3 | -8.0 | -7.8 |
| Net profit before tax | \$M | -9.9 | -19.0 | -22.7 | -13.3 | 2.9 | 28.4 | 55.0 | 133.3 | 144.9 |
| Tax expense | \$M | - | - | - | - | - | - | - | -23.2 | -43.5 |
| Net profit after tax | \$M | -9.9 | -19.0 | -22.7 | -13.3 | 2.9 | 28.4 | 55.0 | 110.1 | 101.4 |
| EPS (cps) | cps | -2.7 | -5.2 | -6.2 | -3.6 | 0.8 | 7.7 | 15.0 | 30.0 | 27.6 |

Balance Sheet

| Year End | June | 2014A | 2015A | 2016F | 2017F | 2018F | 2019F | 2020F | 2021F | 2022F |
|-------------------------------|------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Cash and cash equivalents | \$M | 24.0 | 30.8 | 46.0 | 32.6 | 35.5 | 63.9 | 66.3 | 66.3 | 66.3 |
| Other current assets | \$M | 4.6 | 4.2 | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 |
| Non-current assets | \$M | 8.3 | 9.3 | 8.8 | 8.8 | 8.8 | 8.8 | 8.8 | 8.8 | 8.8 |
| Total assets | \$M | 36.9 | 44.4 | 59.0 | 45.7 | 48.6 | 76.9 | 79.4 | 79.4 | 79.4 |
| Current borrowings | \$M | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other current liabilities | \$M | 3.8 | 6.7 | 9.6 | 9.6 | 9.6 | 9.6 | 9.6 | 9.6 | 9.6 |
| Non-current borrowings | \$M | 0.0 | 0.0 | - | - | - | - | - | - | - |
| Other non-current liabilities | \$M | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Totals liabilities | \$M | 3.9 | 6.8 | 9.6 | 9.6 | 9.6 | 9.6 | 9.6 | 9.6 | 9.6 |
| Net assets | \$M | 33.0 | 37.6 | 49.4 | 36.1 | 39.0 | 67.3 | 69.7 | 69.7 | 69.7 |
| Contributed equity | \$M | 140.3 | 160.9 | 193.5 | 193.5 | 193.5 | 193.5 | 193.5 | 193.5 | 193.5 |
| Reserves | \$M | 4.9 | 7.9 | 9.8 | 9.8 | 9.8 | 9.8 | 9.8 | 9.8 | 9.8 |
| Retained profit/ losses | \$M | -112.3 | -131.2 | -153.9 | -167.2 | -164.3 | -136.0 | -133.6 | -133.6 | -133.6 |
| Total equity | \$M | 33.0 | 37.6 | 49.4 | 36.1 | 39.0 | 67.3 | 69.7 | 69.7 | 69.7 |

Cash Flow

| Year End | June | 2014A | 2015A | 2016F | 2017F | 2018F | 2019F | 2020F | 2021F | 2022F |
|---------------------------------------|------------|-------------|--------------|--------------|--------------|-------------|-------------|--------------|---------------|---------------|
| Cash received from products & service | \$M | 0.4 | 0.5 | 4.1 | 8.0 | 21.9 | 44.6 | 64.2 | 135.3 | 150.4 |
| Payments to suppliers | \$M | -16.1 | -19.3 | -26.0 | -26.1 | -26.8 | -24.5 | -16.3 | -8.0 | -7.8 |
| Net interest | \$M | 1.2 | 1.0 | 0.7 | 0.8 | 1.5 | 1.8 | 1.8 | 1.8 | 1.8 |
| Grants and rebates | \$M | 4.7 | 4.2 | 3.4 | 4.0 | 6.3 | 6.5 | 5.4 | 4.3 | 0.5 |
| Net tax | \$M | - | - | - | - | - | - | - | -23.2 | -43.5 |
| Cash from operations | \$M | -9.8 | -13.6 | -17.8 | -13.3 | 2.9 | 28.4 | 55.0 | 110.1 | 101.4 |
| Cash from investing activities | \$M | -0.3 | -0.7 | 0.0 | - | - | - | - | - | - |
| Net cash from issue of shares | \$M | 0.2 | 20.5 | 32.6 | - | - | - | - | - | - |
| Net cash from borrowing | \$M | - | - | - | - | - | - | - | - | - |
| Dividends paid | \$M | - | - | - | - | - | - | -52.6 | -110.1 | -101.4 |
| Other financing cash flows | \$M | -0.0 | -0.0 | -0.0 | - | - | - | - | - | - |
| Cash from financing activities | \$M | 0.2 | 20.5 | 32.6 | - | - | - | -52.6 | -110.1 | -101.4 |
| Net increase / decrease in cash | \$M | -9.9 | 6.2 | 14.8 | -13.3 | 2.9 | 28.4 | 2.4 | - | - |
| Cash at beginning of the year | \$M | 33.8 | 24.0 | 30.8 | 46.0 | 32.6 | 35.5 | 63.9 | 66.3 | 66.3 |
| Exchange rates | \$M | 0.0 | 0.6 | 0.3 | - | - | - | - | - | - |
| Cash at end of year | \$M | 24.0 | 30.8 | 46.0 | 32.6 | 35.5 | 63.9 | 66.3 | 66.3 | 66.3 |

Valuation

| | | |
|-----------------------|-------|--------|
| Risk free rate | % | 4.6% |
| Market premium | % | 5.5% |
| Beta | x | 1.6 |
| Discount rate | % | 13.4% |
| Forecast period | years | 12 |
| 12-month price target | \$ | \$1.00 |
| Current price | \$ | \$0.70 |
| Return | % | 44% |

SOURCE: Company reports and Canaccord Genuity estimates

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Investment Recommendation

Date and time of first dissemination: August 29, 2016, 02:30 ET

Date and time of production: August 29, 2016, 02:30 ET

Target Price / Valuation Methodology:

Starpharma Holdings Limited - SPL

Our price target is based on a 12-year discounted cash flow valuation (13.4% WACC, 1.6 beta, no TGR) of risk-adjusted royalty and milestone payments that SPL may receive from products developed using its proprietary dendrimer polymer technology.

Risks to achieving Target Price / Valuation:

Starpharma Holdings Limited - SPL

A significant proportion of our valuation is based on commercial development of VivaGel which is currently in Phase-3 clinical trials for the treatment of bacterial vaginosis. If these trial fail to achieve a clinically meaningful benefit, it will have a significant impact on our valuation. Similarly, the value of the dendrimer formulation technology requires those products to successfully complete several clinical trials and secure regulatory approvals. Finally, the commercial development of most of SPL product is based on current and future partnerships. If the company is unable to secure these, or they are secured on financial terms different to what we have forecast, or the partner does not effectively proceed with commercialising SPL's products, it will impact on the valuation of SPL.

Distribution of Ratings:

Global Stock Ratings (as of 08/29/16)

| Rating | Coverage Universe | | IB Clients |
|-----------------|-------------------|--------|------------|
| | # | % | % |
| Buy | 545 | 59.24% | 33.76% |
| Hold | 294 | 31.96% | 19.39% |
| Sell | 21 | 2.28% | 14.29% |
| Speculative Buy | 60 | 6.52% | 75.00% |
| | 920* | 100.0% | |

*Total includes stocks that are Under Review

Canaccord Genuity Ratings System

BUY: The stock is expected to generate risk-adjusted returns of over 10% during the next 12 months.

HOLD: The stock is expected to generate risk-adjusted returns of 0-10% during the next 12 months.

SELL: The stock is expected to generate negative risk-adjusted returns during the next 12 months.

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12-Month Recommendation History (as of date same as the **Global Stock Ratings** table)

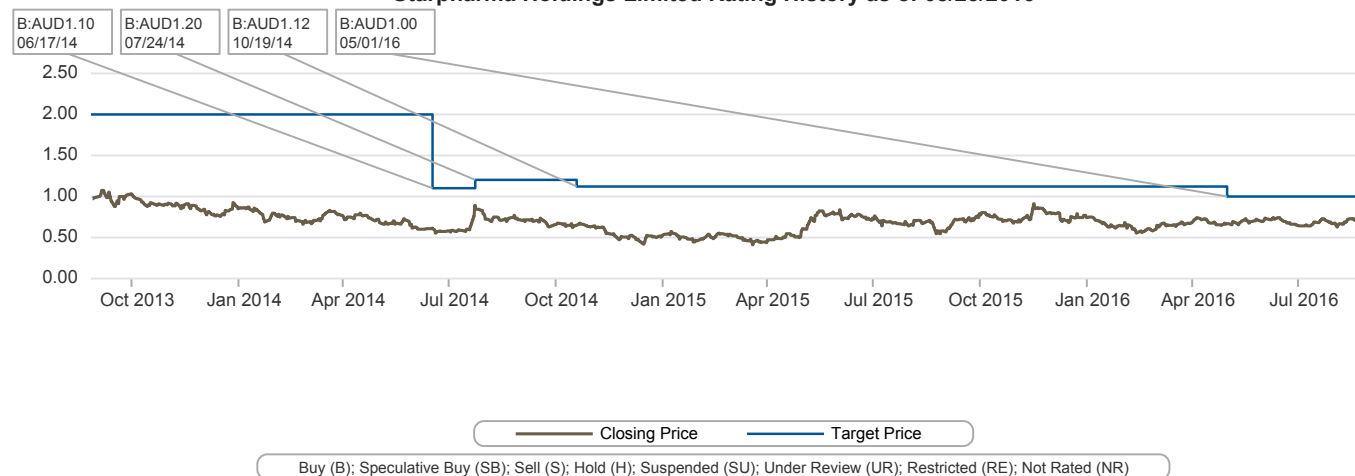
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Starpharma Holdings Limited Rating History as of 08/25/2016**Online Disclosures**

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